

VZCZCXRO7697  
RR RUEHDA  
DE RUEHAK #6744/01 3191456  
ZNR UUUUU ZZH  
R 151456Z NOV 05 ZDK  
FM AMEMBASSY ANKARA  
TO RUEHC/SECSTATE WASHDC 1215  
INFO RUEHIT/AMCONSUL ISTANBUL 9024  
RUEHDA/AMCONSUL ADANA 9960

UNCLAS SECTION 01 OF 03 ANKARA 006744

SIPDIS

SENSITIVE

E AND EB FOR U/S SHINER AND A/S WAYNE  
SIPDIS

E.O. 12958: N/A

TAGS: [ECON](#) [TU](#)

SUBJECT: NEW DIRECTIONS FOR US-TURKEY ECONOMIC RELATIONS

REF: ANKARA 6386

11. (SBU) Summary. Following the last meeting in December 2003, it is Turkey's turn to host the Under Secretary-level U.S.-Turkey Economic Partnership Commission (EPC) in Ankara. Turkey's strong economic recovery since the 2001 financial crisis, notwithstanding large risks of backsliding, creates new opportunities to take our economic dialogue in directions that will help lock-in Turkish growth, support economic change in the region, and open opportunities for U.S. business. An effective agenda for a high-level bilateral economic dialogue should engage a range of U.S. and Turkish economic and foreign policy agencies on energy, economic policy, terrorism finance, regional initiatives, and business development, as well as more "traditional" trade and investment issues. End Summary.

-----  
Turkey's Growth Creates New Opportunities  
-----

12. (SBU) After four years of strong economic performance and the start of EU accession negotiations, Turkey's economy has crossed a watershed. Private sector-led growth based on sound monetary and fiscal policy has brought down inflation, real interest rates, and government debt; spurred capital inflows; led to massive trade growth, private investment and consumption; and created new jobs. Lured by the prospect of EU membership, European, American, Middle Eastern, and Asian investors are once again looking at opportunities in Turkey and driving Turkish asset prices to new highs. For instance, GE Capital's recent acquisition of a \$1.6 billion stake in Garanti Bank is a big bet on Turkey's economic future, as is interest by leading U.S. corporations in Turkey's telecom, energy, automotive, and financial sectors. The resolution of headline commercial disputes involving U.S. companies (e.g., Cargill, Motorola) adds to the positive new atmosphere.

13. (SBU) Turkey's economic success story comes as its strategic importance continues to grow. Economic growth and widening prosperity offers an unprecedented opportunity to (a) lock Turkey into the global economy (showing that market-driven economic success is possible in a Muslim country), (b) turn Turkey into an agent of regional economic growth and change, and (c) open new opportunities for U.S. business that would undergird a durable bilateral relationship. Yet, Turkey's continued success is not assured. Economic reform is incomplete; Turkey's most pressing economic issue is no longer how to return to positive growth, but how to avoid backsliding and sustain strong growth for the many years needed to catch up with its EU partners to be.

-----  
But the Risks Remain Large

-----  
¶4. (SBU) Implementing sound macro policies under an IMF program is easy compared to the microeconomic, 'structural' reforms now needed to sustain growth. The EU process will be a major driver of the tax, banking, social security, agricultural, regulatory, legal and judicial reforms that will keep investment and growth on track. Nevertheless, reforms will shake traditional power relationships and undermine entrenched interests in the traditional corporate realm as well as in the bureaucracies and military. Economic change will create new tensions as millions of hitherto protected agricultural and textile workers are displaced and new entrants into the fast growing workforce clamor for jobs and opportunity. Already harsh regional economic disparities are likely to be aggravated. Turkish Islamists and nationalists remain hostile to foreign investment and privatization. Thus, even as political and human rights reforms create their own tensions, the uncertainties of economic change alone will create myriad opportunities to plunge Turkey back into its economic and political nightmares.

-----  
A New Mix of U.S.-Turkish Economic Engagement  
-----

¶5. (SBU) This new mix of great opportunity and large risks calls for a new mix in our economic engagement with Turkey. Since the financial crisis, our bilateral focus has been on keeping IMF-sponsored economic reforms on track, resolving outstanding trade and investment disputes, and leveling the playing field for new investors. For its part, Turkey has sought concessional access to the U.S. market, notably for

ANKARA 00006744 002 OF 003

its textile exports, even as it keeps its agricultural markets closed and threatens to deprive U.S. pharmaceutical firms of their intellectual property.

¶6. (SBU) A new mix would not neglect the important issues of macro policy and commercial equity. Indeed, it is critical that having resolved some long-standing disputes, Turkey move on to modernize judicial and regulatory infrastructure to ensure that foreign firms are treated equally in the future. A new mix, however, would add (a) greater attention to the micro-policies needed to sustain growth (sharing, for example, U.S. experience with deregulation and employment and income policies), (b) global issues on which Turkey will be a more important player, and (c) new opportunities for expanding regional economic integration, and for U.S. trade and investment.

-----  
A New Agenda  
-----

¶7. (SBU) Encompassing market access, IPR, and investment issues, the trade dialogue led by USTR and the Turkish Foreign Trade Undersecretariat under the Trade and Investment Framework Agreement (TIFA) will be an important part of a renewed economic dialogue. Post looks forward to an early TIFA Council meeting (perhaps in January 2006). At the same time, trade and investment dialogue is not sufficient. The Economic Partnership Commission (EPC) (which last met in December 2003 under the leadership of former Under Secretary of State Larson and former MFA Under Secretary Ziyal) affords a potential umbrella for an

SIPDIS  
enhanced dialogue with the participation of various U.S. agencies that looks at the following issues:

-- Energy: The impending completion of the BTC project should not mark the end of cooperation on "East-West" and "North-South" gas and oil transport systems that

enhance global energy security and reinforce regional economies. This will require improvement of Turkey's domestic energy investment environment, which also offers local opportunities for U.S. business and clean coal technology, energy efficiency, hydrogen, nuclear, and LNG technologies. DOE and its Turkish counterpart have expressed interest in stronger cooperation. A productive first step could be a visit to the U.S. by Energy Minister Guler (ref).

- Economic Growth: The Turkish system does not have a capacity for generating sound economic policy recommendations, and Turkish politicians reflexively turn to subsidies and transfers to address social objectives. Enhanced economic policy discussion should include not only macro policies, but sharing of U.S. experience on market-led policies that promote job creation, poverty reduction, and reduction of regional economic disparities. Engagement of Council of Economic Advisors staff in addition to Treasury, and perhaps non-USG economists, could support such a discussion.
- Terrorism Finance/Financial Crime: As economic exchanges with the rest of the world grow, so do opportunities for abuse. Turkey does not yet have a robust counter terrorism finance system, lacking for example an independent capacity to designate terrorist groups and a fully effective Financial Intelligence Unit. U.S. Treasury and DOJ have offered greater engagement with the Turks at the working level. Policy-level engagement by State and Treasury, however, is needed to get things done.
- Regional Economies: Turkey's economic linkages with Middle East and Central Asian countries are growing, but remain far less than their potential. Encouraging greater infrastructure, energy, trade, and investment linkages with the region would allow for a greater spillover of robust Turkish growth, particularly to the Middle East. In addition to energy projects, it could be useful to explore the potential for including Turkey in emerging regional economic mechanisms, like the Middle East Free Trade Area.
- Business Development: Despite, or perhaps because of, the multiplicity of bilateral business organizations, U.S.-Turkey private sector linkages remain underdeveloped. U.S. business appears unaware, or wary, of the changed environment in Turkey and Turkish businesses are intimidated by the size of the U.S. market. A new project between the U.S. Chamber of

ANKARA 00006744 003 OF 003

Commerce and the leading Turkish business federation, TOBB, to develop SME connections has received \$400,000 in U.S. funding. This is, however, a small start. Intensified engagement by the U.S. Commerce Department and private sector, perhaps including U.S. subsidiaries in Europe, could help create stronger connections, including institutional connections, between the two business communities. This would also create more effective business-led constituencies for investment oriented judicial and regulatory reforms.

-----  
A Broader-Based Mechanism  
-----

18. (SBU) One reason past EPC's have been unsatisfactory was the bureaucratic mismatch between the U.S. Under Secretary of State for Economic Affairs and the MFA Under

SIPDIS  
Secretary, whose normal portfolio is almost entirely

SIPDIS

political and whose agency has limited economic capacity and sway over economic ministries. There is no easy solution to this problem, but an effective mechanism might be the creatio of issue-oriented working groups led by Turkish line agencies with their counterpart U.S. agencies that report to an umbrella group led by the two Under Secretaries.

SIPDIS

-----  
Comment  
-----

19. (SBU) With a new E in place, we expect the Turkish MFA to come forward with a proposal for an EPC meeting, picking up where the last session left off. We believe that high-level economic dialogue has the potential to make a positive contribution to the bilateral relationship. However, for a dialogue to be effective it will be important to be prepared to come back to the Turks with a new, forward-looking agenda, like the one described above, that effectively engages a range of Turkish economic agencies.

McEldowney